

Message Text

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ACTION ARA-14

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TO SECSTATE WASHDC 2224
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C O N F I D E N T I A L BRASILIA 4863

EO 11652 GDS
TAGS EFIN BR
SUBJECT: BRAZIL'S CAPITAL INFLOWS AND DEBT 1976/1977

REF: BRASILIA A-49, MARCH 25, 1977

1. SUMMARY: JUST-RELEASED CENTRAL BANK ANNUAL REPORT SHOWS BRAZIL'S TOTAL FOREIGN MEDIUM AND LONG-TERM DEBT AT THE END OF 1976 AT \$25.9 MILLION, WELL BELOW THE PREVIOUS ESTIMATE OF \$27.2 MILLION. OUR CALCULATIONS INDICATE THAT THE LATTER FIGURE IS CLOSER TO THE ACTUAL SIZE OF THE DEBT. IT APPEARS THAT BRAZIL BORROWED SIZEABLE AMOUNTS OF SHORT-TERM FUNDS LAST YEAR AND THAT THE EXCESSIVE BORROWING DURING THE MONTH OF DECEMBER WAS MOST LIKELY A WINDOW DRESSING OPERATION. SIMONSEN ESTIMATES THAT THE DEBT AT THE END OF 1977 COULD SURPASS \$30.0 BILLION, WHILE GOVERNMENT OFFICIALS EXPECT AN INCREASE IN THE COST OF BORROWING ("SPREAD"). END SUMMARY

2. ACCORDING TO THE JUST-RELEASED CENTRAL BANK'S ANNUAL REPORT, BRAZIL'S TOTAL FOREIGN DEBT INCREASED BY \$4.7 BILLION DURING 1976, REACHING AN ESTIMATED TOTAL OF \$25.9 BILLION. IN HIS STATE OF THE UNION MESSAGE ON MARCH 1, PRESIDENT GEISEL INDICATED THAT

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THE DEBT AT THE END OF 1976 AMOUNTED TO \$25.2 BILLION (REPAIR). WE WERE THUS SOMEWHAT SURPRISED BY THE LATEST ESTIMATE, WHICH CENTRAL BANK OFFICIALS CONFIRMED, AND HAVE ATTEMPTED TO PROVIDE AN EXPLANATION FOR THE DIFFERENCE. TO DO SO, WE HAVE ANALYZED THE 1976 CAPITAL INFLOW DATA INCLUDED IN THE ANNUAL REPORT. BASED ON THE BREAKDOWN OF THIS INFLOW, BRAZIL'S TOTAL REGISTERED DEBT IN 1976 (WHICH INCLUDES MEDIUM AND LONG-TERM CAPITAL INFLOW OTHER THAN

DIRECT INVESTMENTS AND CHANGES IN THE NET FOREIGN ASSET POSITION
OF COMMERCIAL BANKS) SHOULD HAVE INCREASED BY \$6.5 BILLION, INSTEAD OF

\$4.7 BILLION, AS THE FOLLOWING CALCULATION INDICATES:

(\$ MILLIONS)	
CURRENT ACCOUNT DEFICIT	6,062
MINUS: DIRECT INVESTMENT	-1,010
SUB-TOTAL (1)	5,052
PLUS: INCREASE IN RESERVES	PLUS 2,504
SUB-TOTAL (2)	7,556
MINUS: INCREASE IN NET LIABILITY POSIT--1,100	
TION OF COMMERCIAL BANKS	

TOTAL CAPITAL INFLOW REGISTRABLE AS DEBT 6,456

3. THE DIFFERENCE OF \$1.8 BILLION BETWEEN THE INREASE IN THE REGISTERED DEBT (\$4.7 BILLION) AND WHAT THE INCREASE SHOULD HAVE BEEN (\$6.5 BILLION) IS ATTRIBUTABLE TO TWO FACTORS: (A) DELAYS IN THE REGISTRATION OF FOREIGN CAPTIAL AND (B) INFLOWS OF SHORT-TERM CAPITAL (LESS THAN ONE YEAR IN MATURITY) WHICH ARE DEFINITION-ALLY EXCLUDED FROM BRAZIL'S DEBT DATA. THE DIVISION OF THIS \$1.8 BILLION BETWEEN FACTORS (A) AND (B) CAN ONLY BE GUESSED AT SINCE PROBABLY NOT EVEN THE CENTRAL BANK KNOWS FOR SURE AT ANY ONE TIME THE EXACT AMOUNT OF THE CAPITAL REGISTRATION BACKLOG. HOWEVER, WE KNOW FOR CERTAIN, BASED ON PUBLISHED OFFICIAL RESERVE DATA, THAT THERE WAS A HUGE INFLOW OF FUNDS DURING THE MONTH OF DECEMBER TO THE TUNE OF \$1.4 BILLION. (PUBLISHED RESERVES FOR THE END OF NOVEMBER ARE SHOWN AT \$5.1 BILLION WHILE THE END-OF-THE-YEAR

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IGURE IN THE ANNUAL REPORT IS GIVEN AT \$6.5 BILLION). IT IS THEREFORE SAFE TO ASSUME: (A) THAT MOST OF THE DECEMBER CAPITAL INFLOW WAS NOT REGISTERED BEFORE THE END OF 1976 AND (B) THAT A PORTION OF IT WAS PROBABLY IN SHORT-TERM FORM, AND WOULD NOT BE REGISTERED IN ANY CASE.

4. BASED ON THE ABOVE, THE FOLLOWING CONCLUSIONS MAY BE DRAWN:

(A) THAT BRAZIL DID A SIZEABLE AMOUNT OF SHORT-TERM BORROWING DURING 1976, OF WHICH \$1.1 BILLION WAS THROUGH A SHIFT IN THE NET FOREIGN ASSET POSITION OF COMMERCIAL BANKS AND UP TO \$700 MILLION (DIFFERENCE BETWEEN \$1.8 BILLION AND \$1.1 BILLION IN OTHER FORMS (MAINLY PRE-EXPORT FINANCING AND SHORT-TERM IMPORT FINANCING)). (SEE BRASILIA 0621).

(B) THAT THE LARGE INFLOW OF FUNDS IN DECEMBER WAS MOST LIKELY A WINDOW DRESSING OPEERATION DESIGNED TO PUT A -GOOD FACE" ON THE 1976 BALANCE OF PAYMENTS RESULTS. THE CURRENT ACCOUNT DEFICIT OF \$6,062 MILLION WAS ONLY \$700 MILLION BELOW THAT OF 1975.

5. FINALLY, IN SO FAR AS THE 1977 OUTLOOK IS CONCERNED, FINANCE

MINISTER SIMONSEN WAS QUOTED IN THE WEEKEND PRESS (JUNE 11-12) THAT THE CURRENT ACCOUNT DEFICIT WILL BE ON THE ORDER OF \$4.0-4.5 BILLION. BY ADDING TO THE CURRENT ACCOUNT DEFICIT THE AMORTIZATION OF THE DEBT (\$3.5 BILLION), AND DEDUCTING DIRECT INVESTMENTS (\$1.0-1.2 BILLION), THE MINISTER CONCLUDED THAT BRAZIL WILL NEED TO BORROW AN ADDITIONAL \$7.0 BILLION ON THE GROSS BASIS, DURING THE YEAR. (FI DIRECT INVESTMENTS DO IN FACT REACH \$1.2 BILLION, TOTAL NEW BORROWING WOULD BE REDUCED TO \$6.8 BILLION, ASSUMING A CURRENT ACCOUNT DEFICIT OF \$4.5 BILLION). WHILE IN ABSOLUTE TERMS THE 1977 BORROWING REQUIREMENT SEEMS LARGE, COMPARED WITH 1976 IT COULD MEAN AN IMPROVEMENT OF AROUND \$3.0 BILLION. SIMONSEN WAS NOT CONCERNED ABOUT RAISING THIS ADDITIONAL SUM AND NOTED THAT BRAZIL HAS ALREADY BORROWED \$2.0 BILLION. THE MINISTER ALSO ESTIMATED THAT THE TOTAL FOREIGN DEBT AT THE END OF 1977 COULD SURPASS \$30.0 BILLION

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THE PRESS REPORTED, IN ADDITION, THAT MOST OFFICIALS BELIEVE THAT THE "SPREAD" OVER LIBOR (PRESUMABLY ON GOVERNMENT-GUARANTEED LOANS)
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IS LIKELY TO GO UP TO 2.0 PERCENT DURING THE SECOND HALF (IT IS NOW BETWEEN 1.75 AND 1.875 PERCENT). THE "SPREAD" HAS BEEN AT 2.0 PERCENT FOR SOME TIME ON PRIVATE DEBTS.
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